

**REVIEW OF THE INFLATION FACTOR FOR
THE EDUCATION FINANCE ACT**

PRESENTED TO THE

EDUCATION FUNDING STUDY COMMITTEE

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BY

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LEGISLATIVE MANDATE TO THE DIVISION OF RESEARCH AND STATISTICS

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE, THANK YOU FOR GIVING ME THIS OPPORTUNITY TO REPORT TO YOU ON THE STATUS OF THE INFLATION FACTOR FOR THE EDUCATION FINANCE ACT (EFA). THE LAST TIME THAT THE FACTOR WAS REVIEWED BY THE GENERAL ASSEMBLY WAS IN 1990. IT SEEMS TO ME THAT THIS IS A GOOD TIME TO LOOK AT IT AGAIN.

THE LEGISLATIVE MANDATE TO OUR DIVISION IS QUITE CLEAR. IN ACCORDANCE WITH SECTION 59-20-40, "... THE DIVISION OF RESEARCH AND STATISTICS SHALL SUBMIT TO THE LEGISLATURE AN ESTIMATE OF THE PROJECTED RATE OF INFLATION FOR THE FISCAL YEAR TO BE BUDGETED AND THE BASE STUDENT COST SHALL BE ADJUSTED TO INCORPORATE THE INFLATED COST OF PROVIDING THE DEFINED MINIMUM PROGRAM."

THE FIRST ASSIGNMENT THAT I WAS GIVEN WHEN I BEGAN WORKING FOR THE DIVISION IN 1984 WAS TO PROVIDE AN INFLATION FACTOR FOR THE FY 85-86 BUDGET. ON BEHALF OF THE DIVISION, I HAVE PROVIDED THE FACTOR TO YOU EVERY YEAR SINCE THEN.

ESTIMATION OF THE INFLATION FACTOR FROM FY 78-79 TO FY 89-90

THE ORIGINAL METHODOLOGY FOR THE FACTOR WAS ESTABLISHED BEFORE I ARRIVED. THE FACTOR WAS BASED ON AN INDEX OF 88% WAGES AND 12% NON-WAGES TO CORRESPOND TO THE ORIGINAL MODEL OF THE DEFINED MINIMUM PROGRAM. THE WAGE PORTION WAS ADJUSTED BY AN INDEX OF COMPENSATION FOR STATE AND LOCAL GOVERNMENT EMPLOYEES NATIONWIDE COMPUTED BY THE U.S. DEPARTMENT OF COMMERCE. THE NON-WAGE PORTION WAS ADJUSTED BY AN INDEX OF PURCHASES OF GOODS AND MATERIALS BY STATE AND LOCAL GOVERNMENTS NATIONWIDE, ALSO COMPUTED BY THE U.S. DEPARTMENT OF COMMERCE. THAT METHODOLOGY WAS USED THROUGH FY 89-90.

ADOPTION OF SOUTHEAST WAGE INDEX IN FY 90-91

AFTER AN INORDINATE RISE IN THE FACTOR FOR FY 89-90, THE COMMITTEE TO STUDY FORMULA FUNDING, WHICH WAS ESTABLISHED THEN, ASKED US TO RE-EXAMINE THE FACTOR. WE FOUND THAT THE INORDINATE RUN-UP THAT YEAR WAS CAUSED BY A HUGE CHANGE IN PAYMENTS TO THE CALIFORNIA RETIREMENT SYSTEM. THAT WAS A FRINGE BENEFIT ADJUSTMENT. THE U.S. INDEX THAT WE USED FOR THE WAGE PORTION AT THAT TIME INCLUDED FRINGE BENEFITS. THAT WAS A BIT OF A PROBLEM BECAUSE FRINGE BENEFITS WERE NOT PART OF THE ORIGINAL MODEL. THE COMMITTEE ALSO ASKED US TO SEE IF THERE WAS

A WAY TO BRING THE FACTOR "CLOSER TO HOME," RATHER THAN USING A NATIONAL STATISTIC.

WE UNDERTOOK AN EXTENSIVE STUDY AND ISSUED OUR FINDINGS IN JULY 1990. SENATOR SETZLER, I REMEMBER YOU BEING THERE WHEN I PRESENTED OUR FINDINGS TO THE COMMITTEE. I HAVE ATTACHED A COPY OF THAT STUDY FOR YOUR INFORMATION. IT GIVES SOME GOOD HISTORY AT THAT TIME AND I ENCOURAGE THE COMMITTEE TO LOOK AT IT.

WE FOUND THAT THE INFLATION FACTOR UP TO THAT POINT IN TIME DID A CREDIBLE JOB IN ADJUSTING THE COSTS OF THE ORIGINAL MODEL FOR INFLATION. WE ALSO NOTED THAT THE FACTOR DID NOT TAKE INTO ACCOUNT THE COSTS OF UPGRADING TEACHER SKILLS, WHICH WAS AN IMPORTANT CONSIDERATION, BUT NOT INCLUDED IN THE MODEL.

WE RECOMMENDED THAT THE WAGE PORTION BE REVISED TO USE INCREASES IN WAGES OF ALL SCHOOL EMPLOYEES IN THE SOUTHEAST. THIS APPROACH BROUGHT THE INDEX CLOSER TO HOME AND EXCLUDED THE EFFECTS OF FRINGE BENEFITS FROM THE INDEX. IT ALSO FIT WITH THE USE OF THE SOUTHEASTERN AVERAGE TEACHER SALARY. WE FELT THAT WE COULD USE THE RESULTS OF OUR SURVEY OF THE

SOUTHEASTERN STATES FOR INFORMATION ON TEACHER SALARIES TO HELP US IN MAKING PROJECTIONS OF THE EFA INFLATION FACTOR.

AS FOR THE 12% NON-WAGE PORTION OF THE FACTOR, WE DID NOT SEE A PRESSING NEED TO REVISE IT AND LEFT IT ALONE AT THAT TIME.

AT THE DIRECTION OF A PROVISIO PUT IN THE FY 90-91 BUDGET BY THE WAYS AND MEANS COMMITTEE, WE BEGAN USING THE REVISED WAGE FACTOR. I HAVE ATTACHED A COPY OF A LETTER TO YOU, SENATOR SETZLER, THAT WE SENT YOU AS CHAIRMAN OF THE EDUCATION SUBCOMMITTEE THAT BUDGET YEAR, EXPLAINING THE METHODOLOGY IN SOME DETAIL. WE HAVE CONTINUED TO USE THAT METHODOLOGY EVER SINCE FOR THE WAGE PORTION.

BY SURVEYING THE EMPLOYMENT SECURITY COMMISSION OFFICES OF THE SOUTHEASTERN STATES, WE DETERMINED A BASE AVERAGE SALARY OF ALL EMPLOYEES IN THE SOUTHEAST AT \$20,026 FOR FY 89-90. ON THE NEXT PAGE IS THE TABLE THAT DOCUMENTS THE CALCULATION OF THE INFLATION FACTOR SINCE THE REVISION. AS YOU CAN SEE IN COLUMN 1, THE WAGE HAS INCREASED SINCE FY 90-91 TO A PROJECTED LEVEL OF \$34,359 FOR FY 07-08. THE CALCULATION OF THE NON-WAGE PORTION IS SHOWN IN COLUMN 2. TO PUT THIS CALCULATION IN PERSPECTIVE FOR

Preliminary

EFA Factor Computation

Fiscal Year	Average South-East Wage (1)	Non-Wage Index (2)	Index South-East Wage (3)	Composite Index Wages and Non-Wages (4)	Revised Estimate of Base Student Cost to Match Inflation (5)	Estimate of Base Student Cost Provided for Budget (6)	Base Student Cost Approp. (7)	Base Student Cost After Mid-Yr. Cuts by B&CB (8)	Final Base Student Cost, Including S.D.E. Cuts (9)
89-90 a/	20,026	100.0	100.0	100.0	1,467	1,467	1,467		1,467
90-91	21,023	101.0	105.0	104.5	1,533	1,539	1,539		1,539
91-92	21,226	101.1	106.0	105.4	1,546	1,562	1,562	1,505	1,505
92-93	21,737	100.7	108.5	107.6	1,578	1,604	1,585	1,532	1,532
93-94	22,315	104.0	111.4	110.5	1,621	1,651	1,581		1,581
94-95	23,125	107.4	115.5	114.5	1,679	1,652	1,619		1,619
95-96	23,726	106.1	118.5	117.0	1,716	1,718	1,684		1,684
96-97	24,441	110.8	122.0	120.7	1,771	1,778	1,760		1,760
97-98	25,067	112.8	125.2	123.7	1,814	1,839	1,839		1,839
98-99	26,312	114.7	131.4	129.4	1,897	1,879	1,879		1,879
99-00	27,161	118.0	135.6	133.5	1,959	1,937	1,937		1,937
00-01	28,529	121.5	142.5	139.9	2,053	2,012	2,012	1,992	2,002 d/
01-02	29,242	125.6	146.0	143.6	2,106	2,073	2,073	1,940	1,881 c/
02-03	30,574	127.9	152.7	149.7	2,196	2,133	2,033	1,859	1,770 d/
03-04	30,766	130.7	153.6	150.9	2,213	2,201	1,777		1,754
04-05 b/	31,903	133.5	159.3	156.2	2,292	2,234	1,852		1,852
05-06 e/	32,704	137.5	163.3	160.2	2,350	2,290	2,290		2,290
06-07 e/	33,521	142.8	167.4	164.4	2,412	2,367	2,367		
07-08 e/	34,359	148.2	171.6	168.8	2,476	2,476			

Inflation Factor FY08 4.60%

Footnotes and Column Notes:

a/ Base from which increases are computed in accordance with revised methodology.

b/ July 2006 survey, whose latest data is the Average Southeast Wage through 2005.

c/ Reflects mid-year cuts of 5.3% plus S.C. Dept. of Ed.'s additional E.F.A. reduction for allocation to school districts of 3.96% for a net reduction of 9.26%.

d/ Reflects a 1% B&CB cut and a .5% Dept. of Ed. restoration in FY00-01 and a 8.57% mid-year cut in FY02-03.

e/ Estimate based on July 2006 survey and latest two years' average Consumer Price Indexes (see notes b/ & (2))

Source: Budget & Control Board, Office of Research & Statistics

(1) Computed from survey of Employment Security Commission offices in southeastern states based on wage data reported for workman's compensation program. Includes teachers and nonteachers in public schools in the Southeast.

(2) For FY 89-90 through FY 96-97, based on implicit deflator for purchases by state and local governments nationwide as projected by Evans Econometrics. For FY 97-98, based on projection of the Consumer Price Index for the latest two completed years.

(3) Index of column 1 based on FY 89-90.

(4) Column 2 and Column 3 weighted by 12% for Column (2) and 88% for Column (3).

(5) Column 4 times FY 89-90 base amount of \$1,467. Revised after surveys to include actual data.

(6) Original estimate of Base Student Cost.

(7) Base Student Cost appropriated each fiscal year.

(8) Actual Base Student Cost funded to districts after budget cuts by the Budget & Control Board.

(9) Actual Base Student Cost funded to districts after B&CB cuts plus cuts by the State Department of Education.

YOU, THE FACTOR HAS INCREASED AT AN AVERAGE COMPOUND RATE OF 3% OVER THE 18 YEARS SINCE FY 89-90.

ADOPTION OF CPI FOR NON WAGES IN FY 97-98

WE CHANGED THE METHODOLOGY FOR THE NON-WAGE PORTION IN FY97-98. DURING THE 1990'S THE OIL MARKETS BEGAN TO TIGHTEN AGAIN AND WE STARTED EXPERIENCING WIDE FLUCTUATIONS IN THE NON-WAGE PORTION OF THE INDEX. THE NON-WAGE INDEX WE WERE USING, THAT IS, PURCHASES OF GOODS AND MATERIALS BY LOCAL GOVERNMENTS NATIONWIDE, INCLUDED A HEAVY WEIGHT FOR PURCHASES OF PETROLEUM PRODUCTS. AS A RESULT, THE NON-WAGE INDEX BEGAN TO FLUCTUATE WIDELY WITH SWINGS IN OIL PRICES. WE DID NOT THINK THIS WAS APPROPRIATE BECAUSE THE ORIGINAL MODEL DID NOT INCLUDE MUCH FOR FUEL PURCHASES. WE RAISED THIS POINT TO THE APPROPRIATE COMMITTEES AND REVISED THE NON-WAGE PORTION OF THE FACTOR TO THE CPI IN FY 97-98. AS BEST WE CAN TELL, THAT REVISION HAS WORKED OUT OKAY SINCE THEN.

ADOPTION OF TRUE-UP PROCEDURE

WHEN WE ADOPTED THE WAGE REVISION TO THE INDEX IN FY 90-91, WE ALSO ADOPTED THE "TRUE UP" PROCEDURE. AS THE LEGISLATIVE MANDATE SAYS, WE PROVIDE YOU A PROJECTION FOR THE BUDGET. BUT WHAT HAPPENS IF OUR PROJECTION IS WRONG?

THE “TRUE-UP” MEANS THAT WHEN WE GET ACTUAL DATA ON SOUTHEASTERN WAGES TWO YEARS AFTER THE BUDGET PROJECTION, WE REVISE THE FIGURES IN COLUMN 1 TO ACTUAL DATA. THE INTENT IS TO CORRECT THE INFLATION FACTOR IN THE NEXT PROJECTION FOR THE AMOUNT THAT WE MISSED IN PREVIOUS PROJECTIONS. THIS METHODOLOGY WAS INTENDED TO KEEP THE GENERAL ASSEMBLY’S PROMISE TO THE SCHOOL DISTRICTS TO KEEP THEM WHOLE UNDER THE EFA.

WE HAVE KEPT TRACK OF THE “TRUE UP” MECHANISM. THE FACTOR PROJECTED FOR THE BUDGET IS SHOWN IN COLUMN 6 AND THE ‘TRUE-UP’ ESTIMATE IS PROVIDED IN COLUMN 5. FOR FY 04-05, THE LAST YEAR BASED ON ACTUAL DATA, THE “TRUE UP” AMOUNT WAS \$2,292 PER WEIGHTED PUPIL UNIT COMPARED TO THE BUDGET ESTIMATE OF \$2,234 PER PUPIL. WE UNDER PROJECTED THE FACTOR BY \$58 PER WEIGHTED PUPIL UNIT THAT YEAR.

UNDER THE “TRUE UP” PROCEDURE, WE WILL “TRUE UP” THE FACTOR IN THE NEXT PROJECTION, WHICH WILL BE FOR FY 07-08. IF YOU LOOK ON THE TABLE IN COLUMN 6, THE PROJECTED “TRUED UP” FIGURE FOR FY 07-08 IS \$2,476. THAT IS 4.6% OVER THE PROJECTED FIGURE USED LAST YEAR

IN THE BUDGET. OF THIS INCREASE, 0.8% IS DUE TO THE "TRUE UP" FOR FY 04-05 AND 3.8% IS FOR PROJECTED INCREASES IN FY 07-08.

GIVEN THE LEVEL OF THE BASE STUDENT COST, TRUING UP CAN CAUSE QUITE A SHOCK ON THE BUDGET. THE 0.8% TRUE UP THIS YEAR WILL COST THE STATE \$12 MILLION. MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE, I BELIEVE THAT THE COSTS OF TRUING UP HAS GOTTEN TO THE POINT THAT IT IS SIMPLY TOO MUCH FOR THE DIVISION TO BE RESPONSIBLE FOR. I THINK THAT YOU SHOULD TAKE A LOOK AT THIS MATTER. I DID BRING WITH ME A SUGGESTION WHICH I WOULD LIKE TO GO OVER WITH YOU AT THE END OF MY PRESENTATION.

DECLINING IMPORTANCE OF EFA FOR SCHOOL FUNDING

AS ALL OF YOU KNOW, THE EFA ONLY FUNDS A PORTION OF SCHOOL SPENDING. FOR LAST YEAR'S BUDGET WE ESTIMATED THE BASE STUDENT COSTS AT \$2,367 PER WEIGHTED PUPIL UNIT, WHICH AMOUNTED TO \$2,094 PER ADM FOR THE STATE'S SHARE. WE ESTIMATED TOTAL SCHOOL REVENUES AT \$10,776 PER ADM. WE ESTIMATED TOTAL STATE FUNDING AT \$4,357 PER ADM. FROM THESE ESTIMATES, YOU CAN SEE THAT EFA FUNDING WAS APPROXIMATELY 19% OF TOTAL SCHOOL REVENUES AND 48% TOTAL STATE REVENUES.

IN THE FIRST YEAR THAT WE ESTIMATED THE INFLATION FACTOR, THE EFA ACCOUNTED FOR 36.7% OF SCHOOL REVENUES. I HAVE ATTACHED A TABLE SHOWING EFA REVENUES COMPARED TO ALL SCHOOL REVENUES SINCE FY 84-85. AS YOU CAN SEE, THE PERCENTAGE THAT THE EFA ACCOUNTS FOR HAS DECLINED CONTINUOUSLY SINCE FY 84-85. THE TABLE DEPICTS ACTUAL REVENUES REPORTED BY THE STATE DEPARTMENT OF EDUCATION FOR FY 04-05 AT 17.8% OF TOTAL REVENUES. I SHOULD REMIND YOU THAT AFTER FY 04-05 YOU INCREASED FUNDING FOR THE EFA BACK TO THE LEVEL THAT WE PROJECTED, WHICH WOULD EXPLAIN MUCH OF THE DIFFERENCE BETWEEN THE PROJECTED FIGURE I GAVE YOU IN THE LAST PARAGRAPH AND THE ACTUAL FIGURE IN THE TABLE.

DOES THIS DECLINE IN THE DEPENDENCE ON THE EFA MEAN THAT WE HAVE UNDER ESTIMATED THE INFLATION FACTOR? I DON'T THINK SO. IN FACT, THE BASE STUDENT COST TODAY IS, IN MY JUDGMENT, ADEQUATE TO BUY THE ORIGINAL DEFINED MINIMUM PROGRAM AT THE SKILL AND EFFICIENCY LEVELS THAT EXISTED BACK IN 1976. I THINK THAT WE HAVE DONE A REASONABLY GOOD JOB IN ESTIMATING STRICTLY INFLATION.

IN MY VIEW, THERE WAS MORE TO KEEPING THE ORIGINAL MODEL UP WITH THE TIMES THAN STRICTLY INFLATION. THE INFLATION FACTOR DOES NOT TAKE INTO ACCOUNT IMPROVEMENTS IN SKILLS AND

EFA & FRINGE BENEFITS SCHOOL REVENUES FY 1984-85 TO FY 2004-05

1	2	3	4	5	6	7
Year	Total School Revenues /a	EFA School Revenues	EFA % of Total (col 3 / col 2)	State General Fund Fringe Benefits Revenues Paid to Schools /d	EFA and Fringe Benefits School Revenues (col 3 + col 5)	EFA & Fringe % of Total (col 6 / col 2)
1984 -85	1,657,990,839	608,590,769 /b	36.7%			
1985 -86	1,767,705,255	628,331,719 /b	35.5%			
1986 -87	1,915,994,012	647,365,150 /b	33.8%			
1987 -88	2,244,624,915	692,473,448 /b	30.9%	161,571,662	854,045,110	38.0%
1988 -89	2,431,852,885	718,677,999 /b	29.6%	171,364,443	890,042,442	36.6%
1989 -90	2,655,963,207	761,995,181 /b	28.7%	197,103,585	959,098,766	36.1%
1990 -91	2,837,124,456	797,526,012 /b	28.1%	242,672,421	1,040,198,433	36.7%
1991 -92	2,885,073,257	788,956,297 /b	27.3%	240,019,070	1,028,975,367	35.7%
1992 -93	3,030,796,771	808,685,749 /b	26.7%	236,281,924	1,044,967,673	34.5%
1993 -94	3,160,149,892	838,814,468 /b	26.5%	246,068,188	1,084,882,656	34.3%
1994 -95	3,360,184,261	862,625,272 /b	25.7%	248,835,711	1,111,460,983	33.1%
1995 -96	3,572,455,899	896,487,300 /b	25.1%	233,608,920	1,130,096,220	31.6%
1996 -97	3,815,248,355	942,950,186 /b	24.7%	241,192,350	1,184,142,536	31.0%
1997 -98	4,064,288,105	1,006,508,468 /b	24.8%	249,669,461	1,256,177,929	30.9%
1998 -99	4,314,877,766	1,078,080,282 /c	25.0%	263,965,412	1,342,045,694	31.1%
1999 -00	4,804,962,432	1,114,273,990 /c	23.2%	282,317,644	1,396,591,634	29.1%
2000 -01	5,319,985,801	1,152,028,357 /c	21.7%	333,217,175	1,485,245,532	27.9%
2001 -02	5,486,388,294	1,088,755,840 /c	19.8%	357,985,773	1,446,741,613	26.4%
2002 -03	5,613,967,589	1,032,204,791 /c	18.4%	368,584,852	1,400,789,643	25.0%
2003 -04	5,847,784,092	1,027,981,967 /c	17.6%	368,574,785	1,396,556,752	23.9%
2004 -05	6,144,502,761	1,093,602,433 /c	17.8%	373,626,680	1,467,229,113	23.9%

Source: SDE Statement of Revenues (All School Districts including Special Districts)

/a Total School Revenues (col 2.) for FY1985 to FY1998, excludes Interfund Transfers, Bonds and Leases (All other Other Sources accounts were included in Local Sources in these years). For FY 1999 to FY 2005, excludes Intergovernmental Revenue and Other Sources. (See footnotes for account codes)

/b Excludes revenue accounts 1960-1980 (Bonds, Leases and Interfund Transfers)

/c Excludes all revenue accounts in the 2000s (intergovernmental revenues) and 5000s (Other Sources - bonds, leases, interfund transfers, and miscellaneous).

/d SDE Statement of Revenues "Fringe Benefits Employer Contribution" Revenue Code 3180; Includes All Regular School Districts, DJJ & Corrections

Note: DOES NOT include fringe benefits paid through other programs.

EFFICIENCY, COMMONLY CALLED PRODUCTIVITY BY ECONOMISTS. I DID BRING WITH ME A SUGGESTION ON THIS MATTER THAT I WILL PROVIDE AT THE END OF MY PRESENTATION.

TREATMENT OF FRINGE BENEFITS

AS I NOTED EARLIER, THE ORIGINAL MODEL DID NOT INCLUDE FRINGE BENEFITS. WHEN THE EFA WAS ENACTED, FRINGE BENEFITS WERE PAID FULLY BY THE STATE. THERE WAS NO NEED TO INCLUDE THEM IN THE SHARING FORMULA. BUT OVER TIME, THE SHARE OF FRINGE BENEFITS FUNDED BY THE STATE DECLINED. IN FY 94-95, THE STATE BEGAN A PROGRAM TO PHASE IN FRINGE BENEFITS INTO THE FORMULA WITHOUT A CORRESPONDING CHANGE IN THE LOCAL MATCH REQUIREMENT. THE PHASE-IN WAS COMPLETED IN THE FY 98-99 BUDGET. BEGINNING IN THAT YEAR, A DISTRICT'S "FRINGE" ALLOCATION WAS COMPUTED AS A CONSTANT PERCENTAGE OF ITS STATE ALLOCATION UNDER THE BASE STUDENT COST. BY USING THIS ADD-ON PERCENTAGE FACTOR, THE LOCAL MATCH REQUIREMENT IS DETACHED FROM THE FRINGE BENEFIT POT OF MONEY.

THE ATTACHED TABLE ALSO DEPICTS THE EFA AS A PERCENTAGE OF TOTAL SCHOOL FUNDING WITH FRINGE BENEFITS INCLUDED. AS YOU CAN SEE IN COLUMN 7, THE SHARE OF SCHOOL FUNDING WITH FRINGE INCLUDED HAS DECLINED FROM 35.9% IN FY 87-88 TO 23.9% IN FY 04-05.

THE EFA NOW INCLUDES ALLOCATIONS SHOWN IN COLUMN 3 THAT HAVE A LOCAL MATCH ASSOCIATED WITH THEM AND ALLOCATIONS IN COLUMN 6 THAT DO NOT HAVE A LOCAL MATCH ASSOCIATED WITH THEM. I SUGGEST THAT THE COMMITTEE TAKE A LOOK AT THIS HYBRID STRUCTURE.

IMPACT OF PROJECTIONS OF WEIGHTED PUPIL UNITS

MY EXPERIENCE OVER THE LIFE OF THE EFA IS THAT YOU CANNOT SEPARATE THE ASSESSMENT OF THE INFLATION FACTOR FROM A RE-EVALUATION OF THE DETERMINATION OF THE WEIGHTED PUPIL UNITS. LETS FACE IT, THE CALCULATION OF THE POT OF MONEY THAT GETS "SHARED" UNDER THE FORMULA IS BASED ON THE PROJECTED INFLATED BASE STUDENT COST AND THE PROJECTED NUMBER OF WEIGHTED PUPIL UNITS.

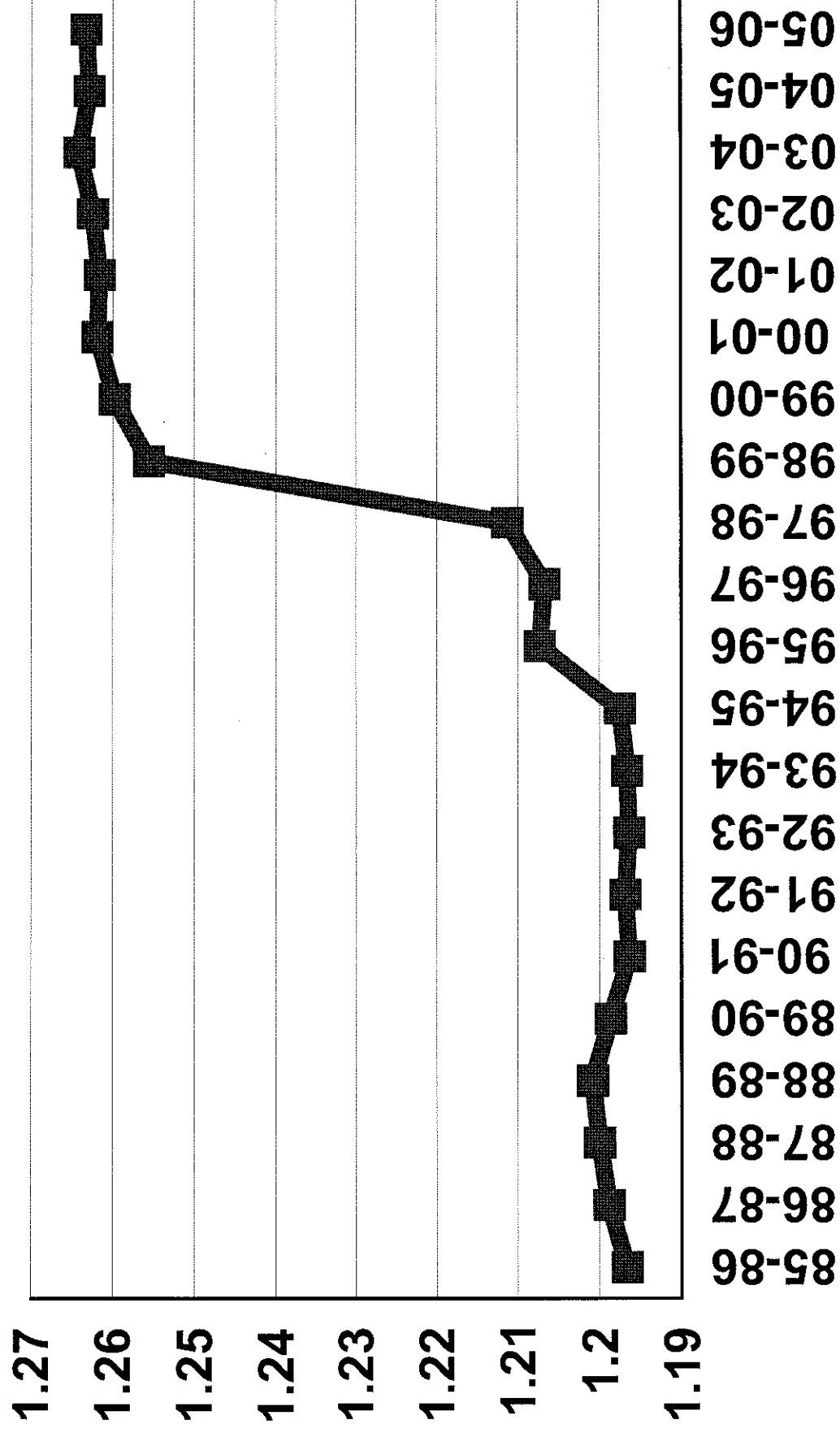
THERE IS NO LEGISLATIVE MANDATE FOR THE DIVISION TO PROVIDE THE GENERAL ASSEMBLY WITH A PROJECTION OF THE WEIGHTED PUPIL UNITS. I CAN'T REMEMBER THE YEAR THAT WE STARTED DOING THE WPU ESTIMATES FOR THE BUDGET, BUT IT WAS AROUND THE MID-1980'S. BACK THEN, ANY EXCESS FUNDING FOR THE EFA AT THE END OF THE YEAR WAS ALLOCATED TO SCHOOL BUILDING. IT WAS A SIMPLE MATTER TO GET FUNDS FOR SCHOOL BUILDING BY JUST OVER STATING THE WPU

ESTIMATE. IT WAS IN THAT ENVIRONMENT THAT THE WAYS AND MEANS COMMITTEE ASKED US TO MAKE THE WEIGHTED PUPIL UNIT PROJECTION FOR THE BUDGET, AND WE HAVE BEEN DOING IT EVER SINCE.

IT'S NOT AN EASY TASK TO MAKE ACCURATE PROJECTIONS OF THE WPU'S. IN MAKING THE PROJECTION, WE TAKE INTO ACCOUNT BIRTHS, INFANT DEATHS, COHORTS, DROP OUTS, TRANSFERS TO AND FROM THE PRIVATE SCHOOLS, THE TREND IN HOME SCHOOLING, AND MIGRATION IN AND OUT OF THE STATE. IN RECENT YEARS, GETTING A HANDLE ON MIGRATION HAS BEEN A HUGE PROBLEM FOR US. WE WILL BE INCREASING OUR PROJECTION OF WPU'S SIGNIFICANTLY FOR THIS UPCOMING BUDGET TO COVER A PREVIOUS UNDER PROJECTION OF MIGRATION AND TO COVER EVEN MORE MIGRATION.

ONE OF THE BIGGEST PROBLEMS WE HAVE HAD IN MAKING THE PROJECTION OF WPU'S IS WHAT WE CALL THE RATIO OF WPU'S TO AVERAGE DAILY MEMBERSHIP (ADM). THIS RATIO REFLECTS THE AGGREGATE MIX OF THE WEIGHTED CLASSES. THE GRAPH ON THE NEXT PAGE DEPICTS THE RATIO OF WPU'S TO ADM'S. IT HAS RISEN FROM 1.19 IN FY 85-86 TO OVER 1.26 IN FY 05-06. THE LARGE JUMP IN FY 98-99 WAS FOR THE INCLUSION OF KINDERGARTEN. THE INCREASE APART FROM KINDERGARTEN FROM FY 85-86 TO FY 05-06 WAS .021. THIS DOESN'T

RATIO WPU'S TO ADM'S



SOUND LIKE MUCH, BUT WHEN SPREAD OVER THE 677,000 ADM'S, IT TOTALS UP TO NEARLY \$25 MILLION.

THERE HAVE BEEN SOME YEARS IN WHICH THERE WAS A PROBLEM WITH THE RATIO PROJECTION. TAKE FY 95-96 FOR INSTANCE. YOU CAN SEE THE SIGNIFICANT JUMP ON THE GRAPH. AT THE END OF THAT YEAR WHEN THE FINAL EFA AMOUNT WAS DETERMINED, WE HAD UNDER-FORECASTED THE BUDGET AMOUNT BY ABOUT \$5 MILLION. NATURALLY, THE STATE DEPARTMENT OF EDUCATION CAME TO THE GENERAL ASSEMBLY WANTING THE \$5 MILLION IN THE NEXT BUDGET.

AND, OF COURSE, I HAD TO REPORT TO THE SENATE FINANCE COMMITTEE ON THE MATTER. WHAT WE FOUND WAS THAT THERE WAS A SIGNIFICANT INCREASE IN THE NUMBER OF STUDENTS CLASSIFIED AS SPEECH HANDICAPPED. I WAS TOLD PRIVATELY BY SOME LOCAL SCHOOL OFFICIALS THAT THEY DID AGGRESSIVELY CLASSIFY CHILDREN INTO THE HIGHER WEIGHTED CLASSIFICATIONS IN ORDER TO INCREASE THEIR EFA FUNDING. IN THAT YEAR THE SENATE CHOSE NOT TO MAKE UP THE SHORTFALL, BUT THE HIGHER WEIGHTED MIX WAS CARRIED FORWARD INTO SUBSEQUENT YEARS.

I BRING THIS UP BECAUSE, TO ME, IT SEEMS THAT THE WEIGHTING SCHEME IN THE EFA, NO MATTER HOW GOOD IT IS IN THEORY, IN

PRACTICE HAS PROBABLY OUTLIVED ITS USEFULNESS. I HAVE A SUGGESTION FOR YOU TO CONSIDER ON THIS MATTER WHICH I WILL COVER AT THE END OF MY PRESENTATION.

RECOMMENDATIONS FOR IMPROVEMENTS

MY EXPERIENCE WITH THE EFA OVER THE TWENTY TWO YEARS THAT I HAVE SEEN IT WORK IS THAT IT IS A GOOD SHARING FORMULA OF A GIVEN POT OF FUNDS. I THINK IT NEEDS TO BE BROUGHT UP TO DATE, HOWEVER. HERE ARE MY SUGGESTIONS FOR YOU TO CONSIDER:

1. REBASE THE BASE STUDENT COST AMOUNT

MY FIRST SUGGESTION IS TO REBASE THE BASE STUDENT COST. I DON'T SEE MUCH SENSE IN GOING BACK TO THE ORIGINAL MODEL AND TINKERING WITH IT. LET'S FACE THE FACTS. WHAT IS AT ISSUE HERE IS THE AMOUNT OF MONEY THAT GOES INTO THE POT TO BE SHARED WITH THE POORER DISTRICTS. AS I HAVE SHOWN HERE, EVEN WITH THE INCLUSION OF FRINGE BENEFITS, THE POT HAS BEEN DECLINING RELATIVE TO THE TOTAL AMOUNT OF REVENUES GOING TO EDUCATION. IT'S MY FEELING THAT THE INFLATION FACTOR THAT WE USED WAS DESIGNED TO COVER ONLY INFLATION AND LEFT OUT PRODUCTIVITY, HELPING TO LEAD TO THE DECLINE IN THE DEPENDENCE ON THE EFA. BY REBASING, YOU CAN MAKE UP SOME OF THE DECLINE IN THE IMPORTANCE OF THE EFA.

MOREOVER, IN LIGHT OF THE PROPERTY TAX BILL PASSED LAST YEAR, I CAN SEE SOME JUSTIFICATION FOR PUTTING MORE INTO THE POT TO HELP BALANCE OUT THE DISTRIBUTION OF STATE FUNDS TO THE POORER SCHOOL DISTRICTS. WE RAN SOME SCENARIOS OF A PROPERTY TAX AND EFA DISTRIBUTION SYSTEM FOR VARIOUS MEMBERS OF THE SENATE DURING THE DEBATE ON H.4449 AND IT SEEMS AS THOUGH SOME BALANCING COULD BE ACHIEVED.

REBASING THE BASE STUDENT COSTS WILL ALSO GIVE YOU A MEANS TO DO SOMETHING ABOUT THE HYBRID CALCULATION USED FOR FRINGE BENEFITS.

THIS "REBASE" DOESN'T NEED TO BE COMPLICATED. JUST ADD SOME AMOUNT TO THE BASE STUDENT COST AND ADJUST THE LOCAL MATCH CALCULATION. I CAN'T TELL YOU HOW MUCH THAT AMOUNT SHOULD BE BECAUSE THAT IS A QUESTION OF EQUITY FOR YOU TO WORK OUT.

2. ESTABLISH A MINIMUM PER PUPIL STATE FUNDING AMOUNT

THE INDEX OF TAX PAYING ABILITY IS A FINE CONCEPT FOR REDISTRIBUTING FUNDS TO THE POORER DISTRICTS IN THEORY, BUT IN PRACTICE IT'S NOT PERFECT. SINCE THE BEGINNING OF THE EFA THERE

HAS BEEN THE PROBLEM OF THE OUT-LYING DISTRICT WHOSE PROPERTY TAX BASE IS EXTRAORDINARILY HIGH RELATIVE TO ITS NUMBER OF WPU'S. WHEN IT WAS YORK 2 WITH ITS PUBLIC UTILITY THAT WAS HIGH, IT DIDN'T SEEM TO BE ALL THAT UNFAIR BECAUSE THE UTILITY WAS PAYING THE TAX, AND NOT THE HOMEOWNERS. BUT WITH THE HUGE RUN-UP IN HOME PROPERTY VALUES ON THE COAST, BEAUFORT HAS BECOME THE OUT-LYING DISTRICT. TO ME, BEAUFORT'S SITUATION IS DIFFERENT BECAUSE ITS TAX BASE IS DEPENDENT, IN LARGE PART, ON HOMEOWNERS. INDEED, THEIR PROPERTY VALUES HAVE SHOT UP SINCE THE BEGINNING OF THE EFA, BUT THEIR INCOMES HAVE NOT FOLLOWED. IN THIS SITUATION, THE INDEX OF TAXPAYING ABILITY IS NOT A GOOD MEASURE OF THE DISTRICT'S ABILITY TO PAY. ESTABLISHING A MINIMUM PER PUPIL DISTRIBUTION WILL HELP CORRECT THIS SHORT-COMING OF THE INDEX OF TAXPAYING ABILITY.

3. ADD A PRODUCTIVITY FACTOR TO THE INFLATION FACTOR

EVEN IF YOU REBASE THE BASE STUDENT COST, OVER TIME DEPENDENCE ON THE EFA WILL AGAIN DIMINISH BECAUSE THE INFLATION FACTOR WILL ONLY MEASURE INFLATION. TO HELP PREVENT THIS, I SUGGEST THAT YOU CONSIDER SOME LEVEL OF ADD ON FACTOR TO THE INFLATION FACTOR, TO COVER PRODUCTIVITY. IT SEEMS TO ME

THAT SOMETHING IN THE ORDER OF ONE PERCENTAGE POINT WOULD BE APPROPRIATE.

4. SIMPLIFY THE WEIGHTING STRUCTURE

AS FOR WEIGHTINGS, WHY NOT ESTABLISH A STRUCTURE BASED ON SOME MEASURE OF POVERTY OR SOME MEASURE OF ECONOMIC WELL-BEING, AS IN THE LEAST DEVELOPED COUNTY DESIGNATION. THIS WOULD ELIMINATE THE NEED FOR A LOT OF RECORD KEEPING AND WOULD STILL ALLOCATE MORE FUNDS TO THE DISTRICTS WITH THE CURRENT HIGHER WEIGHTINGS.

5. ESTABLISH AN EFA RESERVE FUND OF 2%

NOW THAT THE AMOUNT OF FUNDS DISTRIBUTED UNDER THE EFA HAS GOTTEN SO LARGE, ANY PROJECTION CORRECTION OR ANY KIND OF ADJUSTMENT IS LIKELY TO HAVE A SIGNIFICANT IMPACT ON THE NEXT BUDGET. I SUGGEST THAT YOU CONSIDER ESTABLISHING A 2% RESERVE TO USE TO COVER PROJECTION MISSES AND BUDGET SHORT-FALLS. THIS WOULD ALLEVIATE THE IMPACT ON THE NEXT BUDGET OF THE "TRUE UP" PROCEDURE.

ADM and WPU for 1990-91 to 2007-08

	ADMs			WPUs			Ratios		
	45-DAY	%change	135-DAY	%change	45-DAY	%change	135-DAY	% change	45-DAY 135-DAY
'90-'91	621,283		618,356		739,904		739,768		1.19093016 1.196346
'91-'92	626,802	0.888%	623,794	0.879%	746,891	0.944%	746,587	0.922%	1.19159094 1.196849
'92-'93	631,622	0.769%	628,142	0.697%	752,413	0.739%	751,490	0.657%	1.19123879 1.196370
'93-'94	634,419	0.443%	630,197	0.327%	755,847	0.456%	754,101	0.347%	1.19139975 1.196612
'94-'95	638,546	0.650%	634,658	0.708%	761,012	0.683%	760,016	0.784%	1.19179008 1.197520
'95-'96	635,348	-0.501%	631,161	-0.551%	763,117	0.277%	761,999	0.261%	1.20109988 1.207297
'96-'97	641,922	1.035%	637,921	1.071%	770,032	0.906%	769,788	1.022%	1.19957235 1.206713
'97-'98	648,088	0.961%	644,504	1.032%	780,623	1.375%	780,676	1.414%	1.20450155 1.211282
'98-'99	652,498	0.680%	648,879	0.679%	787,209	0.844%	814,739	4.363%	1.2064541 1.255610
all-day K			648,899		814,892				
'99-'00	650,354	-0.329%	648,410	-0.072%	815,100	3.543%	816,853	0.259%	1.25331742 1.259779
'00-'01	650,810	0.070%	648,023	-0.060%	816,819	0.211%	817,731	0.107%	1.25508068 1.261886
'01-'02	654,599	0.582%	652,468	0.686%	821,999	0.634%	823,174	0.666%	1.25572885 1.261631
'02-'03	657,639	0.464%	656,898	0.679%	827,033	0.612%	829,298	0.744%	1.25757952 1.262446
'03-'04	664,337	1.019%	661,376	0.682%	836,745	1.174%	836,085	0.818%	1.25951889 1.264160
'04-'05	668,105	0.567%	665,124	0.567%	840,854	0.491%	839,967	0.464%	1.25856486 1.262873
'05-'06	675,237	1.067%	672,560	1.118%	850,182	1.109%	849,620	1.149%	1.25908681 1.263263
'06-'07			677,192	0.671%			855,844	0.733%	1.264444
'07-'08			680,115	1.123%			859,605	1.182%	1.264000
			683,601	0.961%			864,550	1.017%	1.264700

Numbers in Red are Budget Estimates

Numbers in Blue are Current Estimates (revised after budget)